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July 13, 1994

Mr. William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street, NW, Room 222  
Washington, D. C. 20554

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RE: Ex Parte Meetings  
CC Docket No. 94-1 and  
RM 8356

Dear Mr. Caton:

On July 13, 1994 Gary McBee and Kathy Woods representing the United States Telephone Association (USTA) met with Commissioner Ness and Jim Casserly of her staff and with Commissioner Chong and Richard Welch and Kwok Soohoo of her staff regarding the above-referenced dockets. The attached written material was distributed and discussed.

An original and two copies of this ex parte meeting notice are being filed in the Office of the Secretary on July 13, 1994. Please include this notice in the public record of these proceedings.

Respectfully submitted,

A handwritten signature in cursive script that reads "Linda Kent".

Linda Kent  
Associate General Counsel

Attachment

cc: Commissioner Ness  
Commissioner Chong  
Jim Casserly  
Richard Welch  
Kwok Soohoo

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## PRICE CAP REFORM

On February 16, 1994, the FCC released a Notice of Proposed Rulemaking In the Matter of Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1. The FCC sought comments on three broad sets of regulatory reform issues:

The first set concerns the goals of price caps. The Notice asked for comments on refining the goals of price caps that includes such things as considering whether the plan facilitates economic growth, the creation of jobs, the deployment of the national information infrastructure, and the promotion of universal service.

The second set concerns baseline issues, issues of whether to revise the current plan to improve its performance in meeting Commission goals, or to adjust the plan to changes in circumstances.

The third set of issues relates to a possible transition from the baseline price cap plan toward the relaxation of regulatory oversight and rate regulation as competition develops in the market for access services.

USTA believes that a revised price cap plan should be based on the following goals:

**Promote universal service by encouraging the wide-spread availability of telecommunications services at affordable prices;**

**Promote the introduction of new services and technologies by removing existing obstacles in the regulatory process;**

**Encourage the development of a National Information Infrastructure by providing proper incentives and flexibility for LECs to make the large capital investments that will be required;**

**Stimulate economic growth by helping to reduce costs of production and inducing customers to make greater use of telecommunication services;**

**Allow for balanced competition in access markets by recognizing the rapid market changes that are taking place in the LEC industry;**

**Promote the efficient use of the network by ensuring that decisions made by all carriers and their customers approximate decisions made under competitive market conditions;**

**Prohibit unreasonable discrimination but provide the necessary pricing flexibility that would allow reasonable price differentiation based on market conditions; and**

**Minimize regulatory burdens by removing unnecessary rules and restrictions that no longer serve an essential public interest purpose.**

To attain these goals, USTA believes that:

**The profit sharing/low end adjustment mechanism must be eliminated;**

**The FCC must eliminate the codification of all access rate elements except public policy elements;**

**A revised price cap plan must afford increasing LEC pricing flexibility as access markets become more competitive;**

**The LEC productivity factor should be corrected, based on a long-term Total Factor Productivity study;**

**A common line adjustment formula is not necessary under a revised price cap plan;**

**The FCC should not narrow exogenous cost eligibility;**

**LECs must be afforded equal treatment with other access providers under the FCC's rules;**

**There is no reason to increase service quality and infrastructure monitoring requirements;**

**No changes are necessary in the rules governing the sales and swaps of exchanges;**

**The FCC should avoid diminishing LEC incentives by too frequent reviews of the price cap plan; and**

**The gross domestic product-price index should be substituted for the gross national product-price index as the measure of inflation in the price cap formula.**

## **INTERSTATE ACCESS REFORM**

USTA believes that the framework of rules used by the Federal Communications Commission (FCC) to regulate interstate access services has outlived its usefulness. A new framework is urgently needed if the FCC is to achieve its policy goals in an environment of changing technology and growing competition. USTA proposes Interstate Access Reform which is designed to support the following objectives:

- safeguard universal telephone service at affordable rates;**
- promote the introduction of new services and technologies;**
- support regulation that balances the needs of the market place;**
- promote efficient use of the telephone network;**
- encourage development of a national telecommunications infrastructure; and**
- eliminate unnecessary regulatory burdens.**

Access reform must accommodate the dynamics of markets and technology, maintain support flows that make rural telephone service affordable, and ensure fair and equitable treatment for all access competitors.

### **STRUCTURAL FLEXIBILITY**

The FCC's rules currently dictate how access service offerings are structured (e.g. distance sensitive, minutes of use, etc.). The nature and number of these rate elements are specified in the rules that were established at a time when the local telephone company was the only provider of service. That time has long since passed. As the local telephone companies now face a wide range of well financed, virtually unregulated competitors in most of their markets, these rules have become counter productive to the achievement of public policy goals.

USTA has proposed a major reform plan which puts in place a structure to achieve technological and public policy goals and allows Local Exchange Carriers (LECs) to transition to a competitive market place. In order to achieve these goals, USTA's proposal would establish an efficient, streamlined regulatory regime. The proposal establishes a more flexible structure in which the FCC would no longer maintain a list of each and every permissible "service element" - an impossible task in today's

rapidly changing marketplace. The access structure would be based on functional categories, rather than current FCC defined service classifications. USTA proposes classifying services into four categories: Public Policy, Switching, Transport, and Other. The USTA proposal would facilitate the introduction of new services. It would no longer be necessary to classify each proposed new service under the existing rigidly defined rules - a process which has delayed new service approval in the past.

### **PRICING FLEXIBILITY**

USTA proposes that the degree of regulation should be tailored to the level of competition in a particular market area. Current rules allow LECs to segment markets into zones comprised of areas possessing similar traffic density characteristics. As access markets become increasingly competitive, an additional dimension that takes into account market competitiveness is needed. USTA proposes to designate markets as less competitive, transitionally competitive, or very competitive. Rules governing pricing and price management would vary between these market types. Market areas with limited competition would receive the most regulatory oversight. Regulation would be relaxed in transitional markets. Very competitive markets would receive the least regulatory oversight and the most pricing flexibility. To assist in meeting customer requirements, LECs would be able to respond to customer requests for proposals with contracts tailored to meet individual needs.

### **PUBLIC POLICY SUPPORT OBLIGATIONS**

The goal of universal service at reasonable prices has been a cornerstone of many public policy decisions. Universal service has been guaranteed by requiring LECs to serve all customers at rates that do not necessarily reflect costs. The FCC's new pro-competitive policies challenge the established national goal of promoting universal service. Without reforms, the growth of unbalanced competition in exchange markets will jeopardize support for universal service.

To address this paradox, the FCC must develop new policies that strike a balance between competitive entry and continued public policy support. To achieve this balance, USTA proposes to establish explicit support mechanisms and to replace those which may be implicit in current

averaged service prices. USTA believes that all service providers should share in the costs of public policy goals.

#### **TIMING**

USTA proposes that an expedited review of the FCC's access rules be initiated. Properly viewed, the FCC's recent proceedings on local transport and interconnection are merely interim steps. Upon completion of this expedited interstate access charge review, USTA further recommends that a review of the separations process should be initiated. USTA believes that reforms in both of these processes will promote infrastructure development, bring the benefits of true competition to telecommunications consumers, and help America remain competitive in the global economy.

The FCC established a comment cycle for USTA's petition. Comments were filed on November 1, 1993, and reply comments were filed on November 16, 1993.

## **UNIVERSAL SERVICE**

Regulatory paradigms of the past were designed to promote universal telephone services to all citizens through a package of interdependent policy tools. These tools included holding rates for some services below market levels in many areas, the creation of explicit support mechanisms, internal support flows, and carrier of last resort obligations within exclusive franchises. With these regulatory tools, which were part of a form of social contract between regulators and the telecommunications industry, America's local exchange carriers have successfully achieved an average penetration level of over 94%, although penetration to certain segments of society must still be addressed.

The existing package of regulatory tools is no longer sustainable in today's rapidly evolving telecommunications markets. While existing tools may be adjusted or supplemented in some markets, a transition to new mechanisms and a new regulatory paradigm needs to be developed and tested in many markets. Current social contracts are no longer feasible or, in many cases, desirable. Competitive barriers have fallen through numerous technological and regulatory changes. America is at the threshold of a new era.

The hallmarks of USTA's Universal Service Policy are:

**Reliance on market forces, wherever feasible, to establish reasonable prices and guide the development of new services;**

**Availability of universal services to all consumers;**

**Periodic review of services included as part of the Universal Service Policy vision;**

**Deployment of additional telecommunications and information services to schools, libraries, hospitals, and citizens with disabilities;**

**Affordability of targeted services;**

**Incentives for full participation by all providers in an increasingly competitive telecommunications market;**

**Funding universal service obligations in a competitively neutral manner;  
and**

**Ubiquity through market driven infrastructure deployment and carrier of last resort obligations where required.**

USTA continues to support maintaining nationwide geographically averaged toll rates. Geographically averaged toll rates will continue to be critical to the ability of consumers in many areas to access telecommunications and information services and to be a part of the nationwide super-highway.

A dynamic universal service policy can only be achieved through the adoption of new, forward-looking policy tools. The pervasive regulation which has been used in the past to promote universal service should play a limited role in this new policy mix. Extending this traditional approach to new services and capabilities would slow their adoption, would be inconsistent with the development of competition, and could lead to inefficient investments in the wrong technology. Wherever possible, market forces should provide the means to make the policy vision a reality. Where the marketplace cannot be relied upon to meet the universal service objective, a competitively neutral funding mechanism will be needed to ensure the continued provision of the quality and level of service and technological innovation that all consumers expect. Because customers provide neither infrastructure nor services, universal service funding must both compensate providers of last resort for costs they incur to provide universal service and assist low income customers to afford universal service.

USTA supports and applauds Administration and Congressional efforts to promote a nationwide universal service infrastructure, to expand the support for the infrastructure to all providers in a competitively neutral manner, to remove artificial barriers (such as restrictions applied to local exchange carriers in a discriminatory manner) to the introduction of advanced networks, and to streamline regulations that would apply to all service providers. With the appropriate mix of policy tools and competitive incentives, USTA is confident that America will continue to lead the world in the deployment and availability of customer-determined telecommunications services.